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March 28, 2013

Mr. Terry Holliday, Ph. D.
Commissioner of Education
Capital Plaza Tower
500 Mero Street
Frankfort, KY 40601

Dear Commissioner Holliday,

We received your letter containing follow-up questions concerning KSBIT's potential assessments. Many of these questions indicate that while we answered your initial questions as clearly as possible, it's difficult to reduce a complex and technical set of issues down to a Q and A format. In addition, a number of your questions relate to decisions that have not yet been made by the KSBIT Trustees or processes which are not yet completed. For example, the KSBIT Trustees have not voted on the assessments in general or determined the final amount thereof for either pool, and while the deadline for the RFP process for a potential runoff was last week, we are still in the very early stages of analysis. The final novation offers have not yet been submitted. Several other of your questions have litigation implications and are not appropriate to respond to in this format. Accordingly, rather than go through each question we are responding to those which are appropriate at this time.

The first set of questions you asked related to the provision of actuarial services, the interaction with the Kentucky Department of Insurance ("Department") and steps KSBIT took to address the deficit. Under the contract with the Kentucky League of Cities ("KLC"), KLC is expected to contract for actuarial services. KLC does not have an internal actuary and would not be expected to have one. It is prudent and common practice in the insurance industry to contract for services of an outside actuary to provide the necessary independent actuarial expertise. With respect to the deficit, we cannot list in this letter all of the steps over time that KSBIT has taken to deal with deficits. (A partial list of some management actions are outlined in the attachment). However, we can state that KSBIT took many proactive steps to address the deficits. With respect to your question about whether the surplus loans were considered to have addressed the deficit, based on the knowledge of the parties at that time, the answer is yes. This was but one of the steps KSBIT took to try to address the deficits. Another step was raising premiums. With respect to the Department, as the regulatory agency charged with oversight of both the workers compensation and liability self insured pools, the Department has monitored the financial condition of KSBIT since it came under its jurisdiction a few years ago as it does with all entities under its jurisdiction. The Department was involved in approval of the KLC transaction to address the deficits and has continued to require regular updates on the steps KSBIT is taking to address the deficits. The Department also gets regular financial reports and briefings.

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The next set of questions you asked relate to the issue of novation versus a runoff and the form of the runoff. As indicated above, this process is not complete. The KSBIT Board will not be making these decisions until they have all of the information necessary to make an informed decision. However, we can confirm as we have to our members that both a novation and run-off with a third party administrator are under consideration. A formal RFP process to determine the cost of a runoff and who might be the best third party administrator should the KSBIT Board determine this is the best route to follow has been conducted. Until the responses have been reviewed, KSBIT cannot reveal information about the parties in this or the novation bidding process. The decision of the Board on this issue will be presented to the Kentucky Department of Insurance for approval. Information will be posted and made available to members before the approval is obtained. We are also working on a process to inform and provide for member input.

You have also asked a series of questions about a potential assessment. Specifically, you have asked if bonding can be avoided if there is a series of annual assessments. Bonding is a means of financing the assessment and is intended to help the districts. If a district does not wish to use it, they do not have to do so. While annual assessments are a possibility, they would be more costly than one assessment and might not be approved by the Department of Insurance. The Insurance Code appears to require an assessment sufficient to address the entire deficit. Moreover, having the cash on hand allows the Pools to settle claims more efficiently and ultimately saves money for the districts. We are exploring other structures for assessments which might address this concern but are not ready to propose them at this time. We are not sure we understand your question about districts who contest an assessment. It is the position of KSBIT that the costs of protesting would fall on the district refusing to pay the assessment. In the unlikely event the district were successful in such a contest, the assessments of the other districts would increase.

With respect to your questions about payments to KSBA from KSBIT, these amounts were commercially reasonable amounts which were disclosed in the financials. Prior to the KLC taking over the management and administration of the workers compensation and liability funds, KSBA administered them and was reimbursed for the actual expenses of running the funds. These payments and expenses are all recorded in the applicable year's financial statements.

As to your request for services provided and fees charged by KSBA to the districts over a 23 year period, each district knows the services we have provided and the charges for it. Moreover, as it spans 23 years of services to over 174 districts, there is no single document or report which answers it. So, while we could list many services provided such as the development of policies and procedures, legal guidance, and board training it would undoubtedly not be a complete list. Accordingly, this is a question better addressed to each individual district

Given the technical nature of this subject matter which by necessity involves the use of insurance industry and actuarial terminology, superintendents with such questions should contact KSBIT directly as we believe that this direct communication promotes a better understanding of assessment issues as well as matters specific to their district. They may call 1-877-208-5643 or refer to the KSBIT website at www.ksbit.org.

We will, as always, post the questions and responses to our website to permit access by the broadest audience possible.

Sincerely,



William G. Scott
Executive Director

Enclosure
/ka

Recent Actions

By KSBIT Leadership

- Claims outsourced to third party administrator (2006)
- Implemented new underwriting system (2006)
- On-Site Collaboration with Actuary to Set Rates (2006)
- Increased Case Reserves (2006 and 2009)
- Use of case management and pharmacy review to control medical costs (2006)
- Increased loss control staff (2008)



Examples of Additional Actions

By KSBIT Leadership

- Administration Outsourced to KLC January 2010
- KLC Insurance Services loaned \$8,000,000 in form of surplus note to address deficits (2010)
- Change in claims Third Party Administrator (2010)
- Reduction in agent fees and Reinsurance Savings of over \$500,000 (2011)
- Change in actuarial firm (2012)
- 18.5% WC rate increase for 2012-2013